

ICICI Prudential Life Insurance Co. Ltd.

ICICI Prudential (I-Pru) is the largest Pvt Sector insurance player with a market share of 21.9% in the pvt sector and 11.3% share in the overall industry. The company had a persistency ratio of 82.5% and solvency ratio of 320%, one of the best in the industry.

Embedded Value reflects the value of existing & expected profit from past policies in force: I-Pru's FY16 Embedded Value (EV) was ₹13,939cr, comprising of Adjusted Net worth of ₹5,514cr and Value in Force of Existing business at ₹8,426cr. Since insurance is a long-term contract the cash inflow happens over multiple years, while a large part of the expenses occurs in the initial stage. So, Value in force is the value of future cash flows of all the policy in existence, discounted at Risk Free Rate.

Scope for improving VNB margin: The ability to growth new business premium (APE) and improve the margins on that, is another critical factor for valuing an insurance company, the resultant of which is called Value of New Business (VNB). I-Pru has been able to improve its net new business margins from 5.7% of the premium in FY15 to 8% in FY16. The margins are still low compared to others but what gives confidence is the increasing trend. While the APE grew by 9% in FY16 to ₹5,170, the VNB grew by 52.6% to ₹412cr, largely due to improved margins (backed by increasing business from pure protection plans). Further, assuming acquisition cost were reduced by 30% as per the management the VNB would have been ₹710cr for FY16.

Higher stickiness of clients & funds attracts high valuation for insurance companies: Customer stickiness in insurance business is normally higher than other financial services & hence the profitability is also high vis a vi others like AMC business. Another key positive what we observed is the ability to generate higher profit on a given AUM by insurance companies. On an AUM of ₹1.1 trillion, ICICI Prudential reported a PAT of ₹1,653cr in FY16.

The last deal of ICICI Prudential was done valuing the company at ₹32,500cr: ICICI Prudential had sold a 6% stake in Nov 2015, for ₹1,950cr, valuing the company at ₹32,500cr. While the IPO values the company at ₹47,870cr at the upper price band. While part of the rise in valuation can be due to the fact that the company has improved its persistency rates and the new business margins a lot could be attributed to expected future growth.

Valuations & View: At the price of band of ₹300-334 the issue is offered at 3.1x and 3.4x its reported FY16 EV. While the company has enough scope for business growth in the future, **we believe the issue is fully priced in and hence we have a NEUTRAL rating on the issue.**

Key Financials

Y/E March (₹cr)	FY2013	FY2014	FY2015	FY2016
Net Premium Income	13,417	12,283	15,160	18,999
% Growth YoY		(8.5)	23.4	25.3
Total Income	20,255	21,608	33,956	20,228
% Growth YoY		6.7	57.1	(40.1)
PAT	1,516	1,563	1,640	1,653
% Growth YoY		3.1	5.0	0.8
VNB			270	412
VNB Margins%			5.7	8.0
Solvency Ratio%			337	320
RoEV(%)			15.4	15.3
EV			13,822	13,939
Mkt Cap/ EV (Upper Band)				3.4
Mkt Cap/ EV (Lower Band)				3.1

Source: RHP, Angel Research

NEUTRAL

Issue Open: September 19, 2016

Issue Close: September 21, 2016

Issue Details

Face Value: ₹10

Present Eq. Paid up Capital: ₹1,433cr

Offer for sale: 18.1 cr Shares

Amount raised: ₹5,440- ₹6,057crs*

Post Eq. Paid up Capital: ₹1,433crs

Market Lot: 44 Shares

Price Band: ₹300 - 334

Post-issue implied mkt. cap ₹43,060 - ₹47,940cr*

Note: * indicate at a lower end and upper band respectively

Book Building

QIBs	50%
Non-Institutional	15%
Retail	35%

Pre Issue Shareholding Pattern(%)

Promoters Group	93.5
DII's/FII's/Public & Others	6.5

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Issue Details

ICICI Prudential is offering 18.13cr equity shares of ₹10 each via book building route in price band of ₹300-344/share, entirely comprising offer for sale by current promoters ICICI Bank.

Exhibit 1: Shareholding Pattern

Particulars	Pre-Issue		Post-Issue	
	Cr Shares	(%)	Cr Shares	(%)
Promoter Group	1,43.53	100.0	1,27.21	88.6
Employees, Retail & HNI Investors	0	0.0	8.2	5.7
Institutional Investors	0	0.0	8.2	5.7

Source: RHP, Angel Research

Objects of the Offer

- Objects of the Offer are to achieve benefits of listing equity shares on stock exchanges and to carry out the offer for sale. Listing of equity shares will enhance ICICI Prudential's brand name and provide liquidity to existing shareholders. The listing will also provide a public market for the equity shares in India.

About the Company

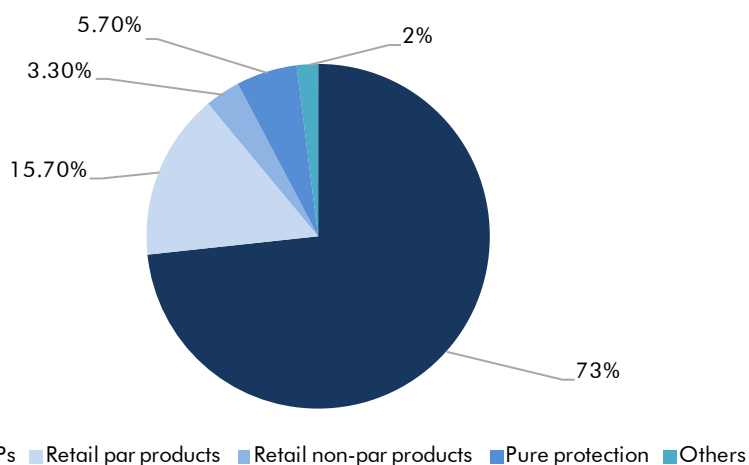
ICICI Prudential Life Insurance (I-Pru) is a JV between ICICI Bank and Prudential Corp. I-Pru commenced its operations in FY2001 and currently offers range of Life & Health Insurance, Pension products to its customers.

In FY2016 I-Pru's market share on Retail Weighted Received Premium (RWRP) basis amongst all Insurance companies was 11.3%, as compared to 9.7% market share of the nearest player.

Amongst 23 private players in Indian Life Insurance space, I-Pru in FY2016 had 21.9% market share. ULIPs accounted for 82.6%/75.2% of I-Pru's Retail Annualized Premium Equivalent (APE) in FY2016/1QFY2017. APE from ULIPs increased from ₹2,210cr in FY2014 to ₹4,179cr in FY2016, representing 37.5% CAGR.

As of June 30, 2016, I-Pru had ₹1.09tn of Assets under Management, making it one of the largest fund managers in India. Of these 73% were in-linked assets. Funds represented 94.2% of linked assets with identified benchmarks as of June 30, 2016, which have performed better than their respective benchmarks since inception. I-Pru's 13th month persistency ratio is at 82.4% for FY2016, one of the highest in the sector. Expense ratio as of FY2016 is at 14.6%, one of the lowest among private sector life insurance companies in India.

Exhibit 2: Product Mix Q1FY17



Source: RHP, Angel Research

Investment rationale

Scope for improving VNB margin: ICICI has been able to improve its net new business margins from 5.7% of the premium in FY15 to 8% in FY16. The margins are still low compared to other players but what gives confidence is the increasing trend. On a APE of ₹5,170cr the company reported a VNB of ₹412cr, and it is worth noting that, assuming acquisition cost were reduced by 30% as per the management believes the VNB would have been ₹710cr for FY16.

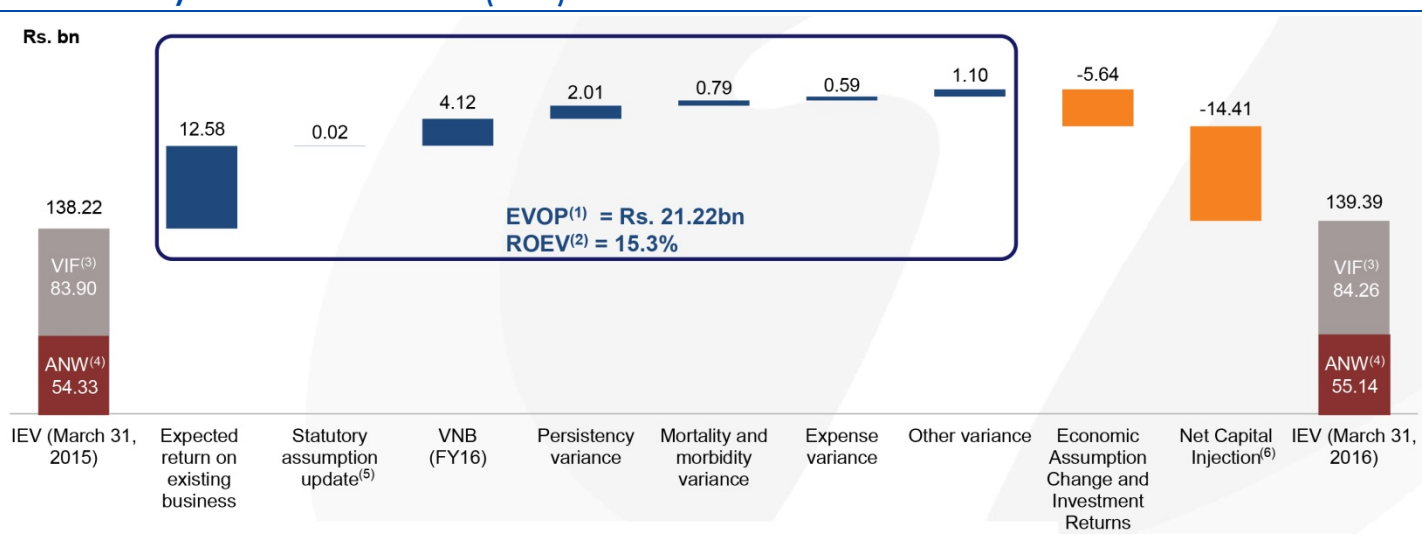
Exhibit 3: New Business Margins

₹ In Cr	FY15	FY16	% Growth YoY
APE	4,744	5,170	9.0%
VNB	270	412	52.6%
VNB Margin	5.7%	8.0%	
VNB, assuming acquisition cost were reduced by 30%		710	

Source: RHP, Angel Research

Embedded Value reflects the value of existing & expected profit from past policies in force: I-Pru's FY16 Embedded Value (EV) was ₹13,939cr, comprising of Adjusted Net worth of ₹5,514cr and Value in Force of Existing business at ₹8,426cr. Since insurance is a long-term contract the cash inflow happens over multiple years, while a large part of the expenses occurs in the initial stage. So, Value in force is the value of future cash flows of all the policy in existence, discounted at Risk Free Rate. The below mentioned table shows the movement of EV for the company in FY16.

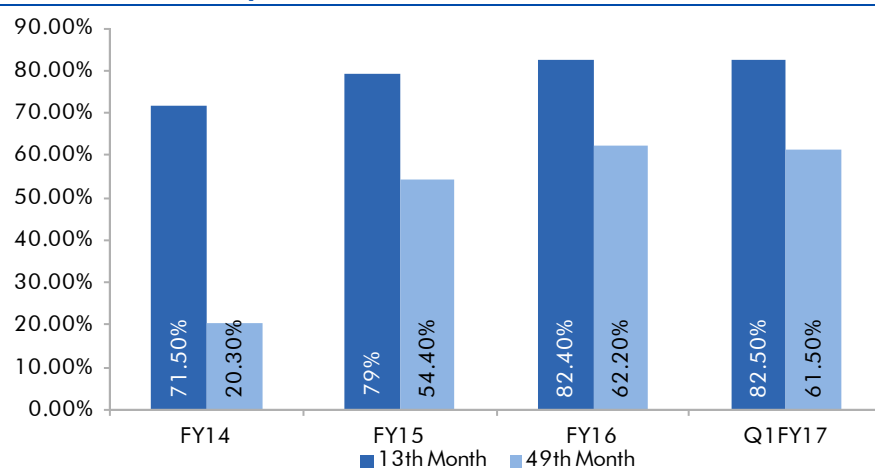
Exhibit 4: Analysis of Movement in IEV (FY16)



Source: RHP, Angel Research

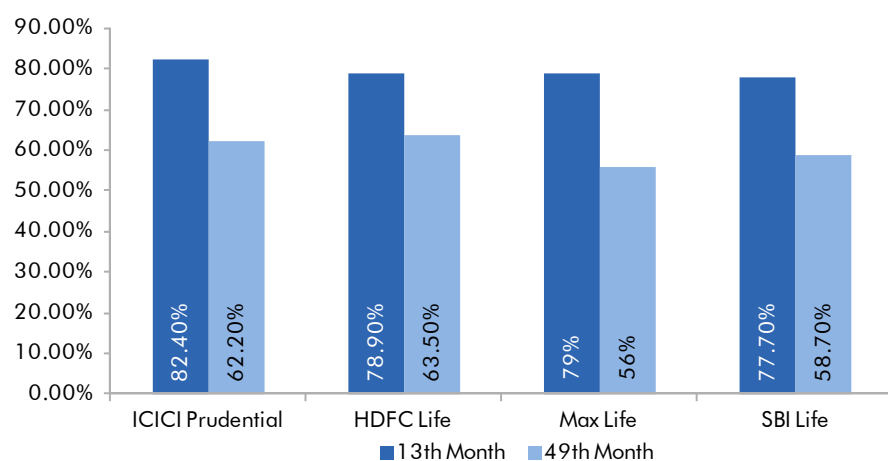
Improving persistency Ratio & Solvency Ratio: The Company has been able to increase the persistency ratio in most of the product category over last few years. The 13th month persistency ratio has gone up from 71.5% in FY14 to 82.5% in Q1FY17, while the 49th month persistency has gone up from 20.3% to 61.5% during the same period. Higher persistency is an indicator of better profitability going ahead. ICICI Prudential has high solvency ratio of 320% compared to the mandatory 150% by the regulator, indicating that the company will be able to meet the business growth without raising capital in the near term.

Exhibit 5: Persistency Ratio Trend



Source: RHP, Angel Research

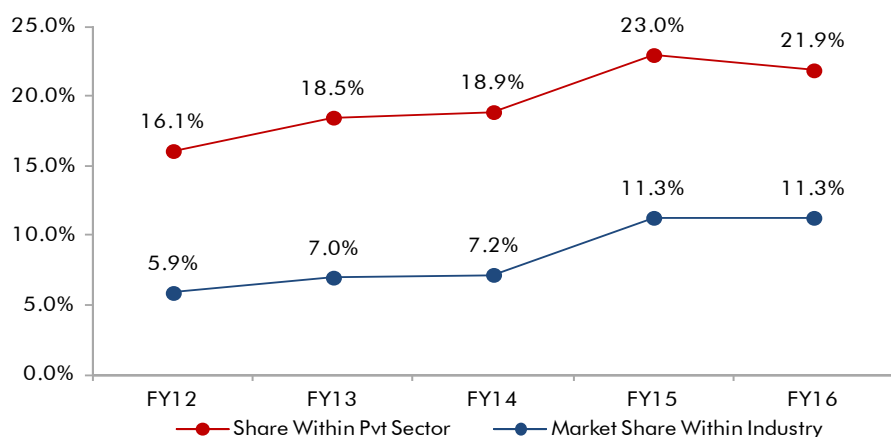
Exhibit 6: Comparative Persistency Ratio



Source: RHP, Angel Research

Higher stickiness of clients and funds attracts high valuation for insurance companies: Customer stickiness in insurance business is normally higher than other financial services, and hence the insurance company is in a position to deploy and generate return on the funds over a long period of time. ICICI Prudential has consistently gained market share, its market share within the pvt industry has gone up from 16.1% in FY14 to 21.9% in FY16, ability to retain market share and improve the persistency ratio could lead to better profitability going ahead. Another key positive what we observed is the ability to generate higher profit on a given AUM by insurance companies. On an AUM of ₹1.1 trillion, ICICI Prudential reported a PAT of ₹1,653cr in FY16

Exhibit 7: Market Share %



Source: RHP, Angel Research

The last deal of ICICI Prudential was done valuing the company at ₹32,500cr

ICICI Prudential had sold a 6% stake in Nov 2015, for a consideration of ₹1,950cr, valuing the entire company at ₹32,500cr. While the current issues values the company at ₹47,870cr at the upper band of the price. While part of the rise in valuation can be due to the fact that the company has improved its persistency rates and the new business margins a lot could be attributed to expected future growth.

Industry Overview

The India life insurance sector is the tenth largest life insurance market in the world and the fifth largest in Asia, according to Swiss Re, sigma No 3/2016. The size for fiscal 2016 was ₹3.7 trillion on a total premium basis.

The Insurance industry in India has undergone transformational changes post 2000, IRDA (Insurance Regulatory and Development Authority) issued license paper to three companies, which are HDFC Life Standard, Sundaram Royal Alliance Insurance Company, and Reliance General Insurance.

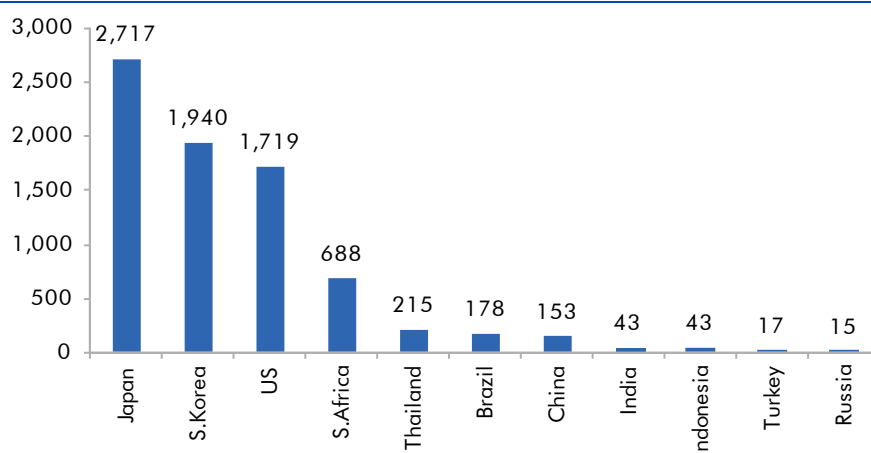
As of March 31, 2016, there are a total of 24 companies in the Indian life insurance sector with LIC being the only public sector life insurer. The private sector has grown significantly since 2000 and it accounted for 51.5% of the life insurance sector, on an RWRP basis, in fiscal 2016.

Recently, The Government increased the maximum permissible shareholding of foreign investors in Indian life insurance companies from 26% of paid-up equity capital to 49% in its Insurance Laws (Amendment) Bill, 2015.

The Indian life insurance is a highly underpenetrated market.

The total premium in the Indian life insurance sector grew at a CAGR of approximately 17% between fiscal 2001 and fiscal 2016. Despite this, India continues to be an underpenetrated insurance market with a life insurance penetration of 2.7% in fiscal 2015, as compared to 3.7% in Thailand, 7.3% in South Korea and a global average of 3.5% in 2015. At US\$43 in fiscal 2015, the insurance density in India also remains very low as compared to other developed and emerging market economies.

Exhibit 8: Insurance Density (In US \$)



Source: RHP, Angel Research

Market Share

The opening up of the sector post-2000, private sector companies have gained significant market share. The financial crisis in 2008 and regulatory changes in fiscal 2010 resulted in loss of market share for private sector companies, and their market share declined to 37% in fiscal 2012.

Private sector companies have regained significant market share in the last two years; increasing their share from 38% of the overall Indian life insurance sector in fiscal 2014 to 52% in fiscal 2016 (on RWRP basis). This growth in market share has been driven by improved product design, primarily for linked products that offer a superior customer value propositions. Private sector companies have also increased their focus on bancassurance for marketing their products.

Product Mix and channel distribution

ULIPs accounted for 92% and 75% of the new business premiums for private sector companies and the overall industry, respectively in fiscal 2008.

There has been a significant shift in the channel mix of the Indian life insurance sector from the earlier agency-only model to a diversified distribution mix. The cap on ULIP charges, introduced in 2010, has led to a rationalisation of owned agency network and introduced a shift towards third-party channels and well-developed banking sector in India and the nationwide presence of banks.

This resulted in the increase of bancassurance share from 5.6% of the retail business, on a new business premium basis, in fiscal 2007 to 24.0% in fiscal 2016, while the share of new business premiums from individual agents decreased from 90.5% in fiscal 2007 to 68.5% in fiscal 2016.

Valuations & View

The Company has disclosed its FY16 Embedded Value (EV) at ₹13,939cr, comprising of Adjusted Net worth of ₹5,514cr and Value In Force of Existing business at ₹8,426cr. At the price of band of ₹300-334 the issue is offered at 3.1x and 3.4x its reported FY16 EV. **While the company has enough scope for business growth in the future, we believe the issue is fully priced in and hence we have a NEUTRAL rating on the issue.**

Balance Sheet

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	Q1FY17
Shareholders' Funds					
Equity	1,429	1,429	1,432	1,432	1,433
Reserves & Surplus	3,412	3,553	3,834	3,893	4,311
Net Worth	4,841	4,982	5,265	5,325	5,744
Policyholder's Fund					
Policy Liabilities	11,028	13,813	17,259	20,255	21,138
Provision for Linked Liabilities	57,389	60,265	74,775	75,295	79,369
Fair Value Change	318	546	1,232	1,029	1,370
Funds for Future Appropriation	508	497	527	662	639
Sources of Funds	74,084	80,103	99,059	102,565	108,260
Investments					
Shareholders	4,919	5,349	5,857	6,216	5,547
Policyholders	11,277	14,443	18,858	21,516	22,972
Asset held for Linked Liabilities	57,521	60,310	74,778	75,296	79,370
Loans	9	12	20	44	50
Fixed Assets	172	202	215	220	213
Net Current Assets	(694)	(810)	(669)	(726)	108
Misc Expenditure	881	597			
Application of Funds	74,084	80,103	99,059	102,565	108,260

Policyholders Account

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	Q1FY17
Premium earned net	13,417	12,283	15,160	18,999	3,509
% YoY Growth		-8.5%	23.4%	25.3%	
Income from Investments	6,187	9,213	18,739	1,208	5,356
Other Income	24	17	18	21	14
Contri. from shareholders a/c	627	96	39		53
Total A	20,255	21,608	33,956	20,228	8,884
% YoY Growth		6.7%	57.1%	-40.4%	
Commission	765	628	553	620	126
Operating Expenses	1,713	1,616	1,654	1,888	552
Benefits Paid (net)	13,293	12,083	12,260	12,425	2,928
Change in valuation of liab.	2,593	5,662	17,956	3,516	4,957
Others	335	320	313	364	94
Provisions for tax	35	48	51	70	0
Total (B)	18,734	20,356	32,788	18,883	8,657
% YoY Growth		8.7%	61.1%	-42.4%	
Surplus/ (Deficit)	1,521	1,252	1,168	1,345	227
Transfer to shareholders A/c	1,773	1,264	1,137	1,210	250

Shareholder's Account

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	Q1FY17
Transfer from Policyholders Account	1,773	1,264	1,137	1,210	250
Income from investments	416	395	537	600	196
Total A	2,189	1,658	1,675	1,810	445
Expenses (aprt from insurance)	6	11	45	31	7
Contribution to policyholders account	627	96	39		5
Others	-	26		4	
Total B	633	134	84	36	13
Profit/ (Loss) before tax	1,556	1,525	1,590	1,774	433
Provision for taxation	41	-38	-50	121	28
Profit (loss) after tax	1,516	1,563	1,640	1,653	405
% YoY Growth		3.1%	5.0%	0.8%	

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